VZCZCXYZ0029
RR RUEHWEB

DE RUEHCH #0227/01 0841329
ZNR UUUUU ZZH (CCY ADX0046FF9F MSI7921)
R 251329Z MAR 09
FM AMEMBASSY CHISINAU
TO RUEHC/SECSTATE WASHDC 7782
INFO RUEHMO/AMEMBASSY MOSCOW 3272
RUEHKV/AMEMBASSY KYIV 0639
RUEHBM/AMEMBASSY BUCHAREST 4327
RUEHSF/AMEMBASSY SOFIA 0690
RUEATRS/DEPT OF TREASURY WASHINGTON DC
RUCPDOC/USDOC WASHDC 0748
RUCPCIM/CIM NTDB WASHINGTON DC

UNCLAS CHISINAU 000227

C O R R E C T E D C O P Y (ADDED CAPTION)

STATE FOR EUR/UMB, EEB/IED, EEB/ESC, EEB/IFD/OMA,
EEB/EPPD
SIPDIS
SENSITIVE

E.O. 12958: N/A
TAGS: ECON EAGR EINV EFIN ETRD PGOV KTDB MD
SUBJECT: MOLDOVA SUCCUMBS TO ECONOMIC CRISIS

REF: CHISINAU 08 1273

¶1. (SBU) Summary: After the GOM's initial confidence that Moldova might ride out the global financial storm (backed by positive economic figures for 2008), more recent news about a slowdown in imports, exports and remittances forebodes gloom for 2009. The International Monetary Fund now projects that the situation is far worse than was initially predicted. The banking sector still seems sound, but there is much speculation about possible devaluation of the national currency after elections. With an economy whose growth in recent years has been driven largely by remittances from migrant workers, Moldova may suffer severely as international markets slide deeper into recession, and some of these workers return home to join the ranks of the locally unemployed. Lower remittances will cause a decrease in local consumption and a consequent decline in imports. And fewer imports will result in a substantial drop in customs duties from which the GOM derives 70 percent of its revenues. Separatist Transnistria has been even harder hit and is in desperate need of support from Russia. The upcoming parliamentary elections on April 5 complicate the situation, since the ruling Party of Communists of the Republic of Moldova (PCRM) is fully focused on the campaign and on keeping up the appearances of a sound economy. Such an approach may prove deleterious after the elections. In the post-electoral period, efforts to put together a ruling coalition may distract political leaders from the need to focus on economic policy as soon as possible. End Summary.

ECONOMIC GROWTH SLOWS AT END OF 2008

¶2. (U) In 2008 the Moldovan economy continued to grow as it has done each year since 2000. During the first three quarters of 2008, the Moldovan economy outperformed the initial projections for the year. The last quarter of 2008, however, saw a deceleration across the board as the global crisis started to bite. Growth reached 10.8 percent in the third quarter, the highest in Moldova's recent history. GDP growth slowed in the fourth quarter, bringing the final annual rate

nevertheless to an impressive 7.2 percent. Agriculture had a spectacular jump of 31.9 percent in growth thanks both to a good harvest and reflecting a recovery from the worst drought in years in 2007. However, the bumper agricultural harvest of 2008 has not helped Moldovan farmers who have had to struggle with low regional commodity prices. Many farmers have chosen to store their crops in warehouses, barns and silos rather than take a loss by accepting the current low prices on agricultural products. Industrial output edged up a disappointing 0.7 percent, while retail soared 8.4 percent.

¶3. (U) MoldovaQs product competitiveness suffered somewhat in 2008 as a result of the depreciation of the currencies of the countryQs main trade partners, in particular in Ukraine and Russia. Nonetheless, the country's export growth remained fairly strong in 2008 at 19 percent. Imports shot up 32.8 percent, further contributing to an ever-widening trade deficit, which equaled 54.6 percent of GDP. Construction was down 8.9 percent, confirming earlier media reports that the construction boom was turning into an outright bust.

TIMES OF TROUBLES AHEAD

¶4. (SBU) Statistical data for the first two months of 2009 are beginning to show signs of trouble ahead for Moldova. The picture will be clearer when first quarter 2009 statistics are released. The slowdown in the final months of 2008 now seems to have been the beginning of a more serious economic crisis, which will be picking up speed during 2009. Industrial output plunged 25.1 percent year-on-year in January 2009. Imports were down 28.2 percent in the same month. Private trucking companies are laying off personnel. Media have revealed copies of managersQ letters at the state-run railway enterprise, suggesting a cut in employeesQ working hours.

¶5. (SBU) At the beginning of March, the IMF included Moldova in the list of 26 countries highly vulnerable to the global downturn but not requiring urgent assistance. The IMF's Resident Representative, Johann Mathisen, told the Embassy that in the first two months of 2009 the IMF registered drops in remittances of 15 to 20 percent over the same months in 2008. Remittances serve as a financial lifeline for many cash-strapped Moldovans. These remittance-dependent Moldovans may find themselves in need of assistance, if the remittances they receive decrease or cease. The state news agency, Moldpress, attempted to put a positive spin on the developments by noting that Moldovans abroad still had jobs and managed to send USD 65 million home in January. The next few months will reveal the true impact of the global downturn on Moldovan migrant workers. Many Moldovans go abroad in spring and summer to work for up to six months before returning home. Party representatives have informed Embassy staff that increasing numbers of migrant workers are returning home and are unemployed. The IMF also noted that imports dropped 50 to 60 percent in February 2009. A drop in imports seriously undermines state budget revenues, of which 70 percent are derived from customs duties. Businesses are noting decreased sales as without remittances Moldovans have less cash to spend. At this rate, the current GOM budget will be unrealistic because it will not receive the planned revenues from customs duties on imports.

¶6. (SBU) The GOM added "election-related" expenses to the budget in the form of wage increases for some government employees, e.g., teachers, at the end of December 2008, an expense that the GOM had not originally planned. The IMF noted that pension increases, anticipated by many citizens shortly before the elections, would be another unplanned expense for the government. When the April 5 elections are over, the new government will face an immediate necessity to rectify the budget. The new government will have to consider reducing government expenditures and will likely need international assistance.

NATIONAL CURRENCY UNDER STRAIN

¶7. (SBU) The GOM seems intent on depleting the National BankQs foreign exchange reserves in order to support the national currency. Since the beginning of 2009 alone, the National Bank has lost 23.5 percent or USD 392.6 million from its foreign exchange reserves by intervening in the currency market to prop up the Moldovan leu. Despite the National Bank's interventions, the leu has lost four percent of its value against the U.S. dollar since the beginning of the year. In the first two weeks of March, exchange offices were overwhelmed by Moldovans wishing to exchange Moldovan lei into foreign currency. Authorities responded by blaming independent economic analysts for unfounded and unprofessional statements about the imminent devaluation of the leu in an effort to calm citizens. Shortly thereafter, the U.S. dollar again dropped below the psychological level of 11 lei to the U.S dollar at exchange offices. Critics of the National Bank's policy have been calling for a gradual devaluation of the leu to boost exports and to make local products more competitive against imports. If the GOM holds to

its course of supporting the leu, imports may pick up. Products from neighboring countries with falling currencies will become cheaper for Moldovans. However, Moldovan exports will likely decrease, if the leu continues to hold steady. Neighboring countries will be unable to purchase increasingly more expensive Moldovan products as their currencies continue to lose value.

RUSSIA HELPS BREAKAWAY TRANSNISTRIA DEAL WITH THE CRISIS

¶8. (SBU) Crippled even more severely by the global economic crisis than right-bank Moldova, the more industrialized breakaway region of Transnistria has slid into a deeper slump. Both industrial output and exports plunged dramatically to almost a half of last year's corresponding figures in the first two months of 2009. The two largest contributors to the Transnistrian budget, the Rybnitsa Metal Plant and Rybnitsa Cement Plant, slashed their output by over 40 percent.

¶9. (U) Authorities in the region have moved quickly to adopt measures to fight the effects of the crisis in the region. The region's authorities were forced to postpone an earlier announced raise in salaries for state employees from March to September 2009. At the same time, Transnistrian authorities froze any increases in prices for utilities (gas, electricity, heating, etc.) at least until September and allowed barter transactions between enterprises.

¶10. (U) The Supreme Soviet, Transnistria's parliament, reported in February that, following earlier appeals by local authorities, Russia

granted about USD 7 million to the region to pay pensions and bolster financing for social and medical facilities. Few details are available about the terms and conditions of Russia's financial and economic support which is packaged as humanitarian aid. This Russian assistance is key to preventing an economic and social collapse in the region. It is Russia's support that helps maintain the Transnistrian ruble's exchange rate, according to Vladimir Yastrebchak, the region's "foreign affairs minister."

COMMENT

¶9. (SBU) The PCRM's focus on the campaign paralyzes the GOM's ability to address the economy in any other manner than to continually reassure citizens that Moldova is doing fine. The ruling party's short-term interests in defeating the opposition parties in the upcoming April 5 elections trump any serious efforts by the current government to alleviate the pending budget crisis. The PCRM has focused most of its electoral campaign on the country's stability and economic growth over the last eight years and chooses to ignore the fallout from the global economic crisis. In an effort to project confidence in its handling of the economy, the GOM did not engage with a recent IMF mission to discuss a new IMF framework to replace the current memorandum that is due to expire in May. The IMF does not expect the government to be in a position to discuss fiscal and monetary policy until after the elections. Moldova could not have been caught at a worst possible moment for the global economic crisis to begin taking a toll on the Moldovan economy. The IMF and other analysts expected Moldova to feel the crisis sharply in the next two or three months. An effective response to the pending crisis in Moldova depends on the outcome of the elections and the expediency with which the new Parliament will be able to elect a President and approve a new cabinet to start dealing with budget shortfalls and the economic issues at hand.
CHAUDHRY